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BEFORE THE
POSTAL REGULATORY COMMISSION
WASHINGTON, D.C. 20268-0001

ANNUAL COMPLIANCE REPORT, 2014	Docket No. ACR2014

REPLY COMMENTS OF
THE NATIONAL POSTAL POLICY COUNCIL
(February 13, 2015)

The National Postal Policy Council ("NPPC") respectfully submits these reply comments on the Postal Service's Annual Compliance Report for Fiscal Year 2014 ("*ACR*"), filed December 29, 2014. NPPC will address certain comments regarding First-Class service performance, and comments of certain parties regarding the Metered Mail rate category in First-Class Mail.[1]

In its initial comments, NPPC pointed out that the *ACR* shows that First-Class Automation and Presort Letters and Cards once again paid an exorbitant cost coverage -- nearly 100 percent higher than the average for First-Class Mail -- and a significantly larger unit contribution than more costly Single-Piece mail, perpetuating a long-standing pattern.[2] The perennial existence of this grossly unfair contribution, which the noticed increases in Docket No. R2015-4 will only aggravate, casts doubt on whether the rate schedule continues to be just and reasonable, as required by Section

[1] *Initial Comments of the American Postal Workers Union*, AFL-CIO (Feb. 2, 2015) ("*APWU Comments*"); *Initial Comments of the Greeting Card Association* (Feb. 2, 2014) ("*GCA Comments*").

[2] *Comments of the National Postal Policy Council* at 2-8 (Feb. 4, 2015); *accord Comments of Pitney Bowes Inc.*, at 1-2 (Feb. 2, 2015).

3622(b)(8) of the Postal Accountability and Enhancement Act ("PAEA"), or satisfies other objectives set forth in Section 3622(b).

NPPC also urged the Commission to consider reducing the price cap applicable to First-Class Mail to offset (1) the recent reductions in service quality – such as the slower service standards resulting from Network Rationalization; and (2) the increased cost of using the mail resulting from the Postal Service's shifting costs to mailers.[3]

I. THE COMMISSION SHOULD ADJUST THE PRICE CAP APPLICABLE TO FIRST-CLASS MAIL TO COMPENSATE FOR SERVICE DECLINES AND COST SHIFTING

While the Postal Service has done a good job of shedding many costs since enactment of the PAEA, in recent years it has developed a tendency to seek cost reductions in improper ways: by reducing service and shifting costs to customers. The recent reductions in both the service standards for, and service performance received by, First-Class Mail, coupled with the Postal Service's propensity to shift costs to mailers rather than improve overall efficiency, justifies an inquiry into whether the price cap applicable to First-Class Mail should be adjusted to a corresponding degree.

The comments of several other commenters were consistent with NPPC's concern. The Public Representative's Comments (at 5-6) highlighted the decline in on-time service performance for every domestic category and delivery time for First-Class Mail. As the Public Representative stated: "Although the Postal Service increased its delivery *standards* by one full day during the 4th quarter of FY2012

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3 *NPPC Comments* at 11-14; *accord Comments of PostCom* at 1-2 (Feb. 4, 2015).

without significantly increasing its performance targets . . . delivery performance in FY2014 nevertheless dropped significantly." *Id*., at 7-8.

In addition, the APWU suggested that First-Class service reductions have had a disproportionate effect on service quality in rural communities. *APWU Comments* at 2-6. First-Class business mailers desire good quality service to all communities. If it were shown that the Postal Service has reduced service in rural areas to cut costs, that action would be relevant to whether it is evading the cap.

A price cap regulatory regime is intended to encourage cost reductions without reducing service. Many of the Postal Service's initiatives have been able to trim costs without a reduction in service, but perhaps the Service has exhausted the low-hanging fruit. It is evident that a First-Class mailer today is not receiving the same service as it received in 2012, let alone 2007. A stamp today does not buy the service or quality that a stamp bought only a few years ago, which constitutes, NPPC submits, an effective rate increase on top of the nominal tariffed rate increases. Therefore, to the extent that the Postal Service has decreased costs by cutting service (or shifting them to mailers), the applicable price cap should be adjusted accordingly.

II. CRITICISMS OF THE METERED MAIL RATE LACK MERIT

Both the APWU and GCA object to the Metered Mail rate category within Single Piece First-Class Mail, arguing that the rate category discriminates against "household" mailers in violation of Section 3622(b)(8). GCA also raises additional concerns under Sections 3622(b)(1) and (b)(5). The Commission should reject these contentions.

A. Background of the Metered Mail Rate Category

The Postal Service established the Metered Mail rate category in Docket No. R2013-10 in response to the Commission's own suggestion that such a rate could usefully serve as an appropriate benchmark from which Presort rates could be set. *See* Docket No. R2013-10, Order No. 1890 at 49 (Nov. 21, 2013); *Consideration of Workshare Discount Rate Design*, Docket No. RM2009-3, Order No. 1320 at 11, n.22. In addition, the Postal Service also identified a number of benefits that it anticipated from the new rate category. These included encouraging small businesses to convert from stamps to meters, customer convenience, operational savings, lower risk associated with stamp theft, and more cross-selling opportunities, which the Commission cited approvingly.[4] *See* Order No. 1890, at 49-51.

The Metered Mail rate has been in effect since January 2014 and serves as the benchmark for the Presort worksharing discounts.[5] Accordingly, it must be fully understood that any upward adjustment to the Metered Mail rate (of the type obviously sought by APWU and GCA) *also* would shift *all* Presort rates upward by a corresponding amount. As an immediate example, the 0.5-cent increase in the Metered Mail rate category noticed in Docket No. R2015-4 will, because it serves as a benchmark, raise the price of the nearly 37 billion Automation and Presort letters by

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[4] The Postal Service noted at that time that the experience of foreign posts provided reason to expect these benefits could accrue from a lower metered letter rate.

[5] Although NPPC recognizes that the Metered Mail rate currently provides this "linkage" to Presort rates under the prevailing interpretation, NPPC continues to maintain its position that Presort Mail is an independent product that simply is not in a worksharing relationship with Single-Piece mail.

that same 0.5-cent amount by itself. And the limitation on passing through costs avoided in workshare discounts means that, where the pass-through already is set at 100 percent, there is little opportunity for relief for Presort mailers.

APWU and GCA both challenged the introduction of the Metered Mail rate in Docket No. R2013-10, and the Commission properly rejected their contentions. Order No. 1890 at 50-51. Because the Commission deferred questions regarding Section 3622(b)(8) to this subsequent review, APWU and GCA have reformulated some of their contentions. But the Commission should again reject them in their new incarnation as well.

B. The Metered Mail Rate Is Not Improper Price Discrimination

APWU and GCA repeatedly refer to the Metered Mail rate category as "price discrimination." Other than in the broad sense that *any* rate difference "discriminates" in some respect (for example, that Standard Mail Carrier-Route Letter rates discriminate against First-Class Presort mailers), it is unclear that the Metered Mail rate category discriminates against household or any other identifiable group of mailers in any way cognizable under the law.

Section 403(c) of the postal law prohibits only "unreasonable" price discrimination. For a price discrimination to be unreasonable, there must be a showing that the complaining party has been offered less favorable rates or terms and conditions than one or more other mailers; that it is similarly situated to the favored mailers; and that there is no rational or legitimate basis for the Postal Service to deny it the more favorable rates or terms offered to others. *Complaint of GameFly, Inc.*, Docket No. C2009-1, Order No. 718 at 28 (April 20, 2011). These conditions are not satisfied here.

The Metered Mail rate is simply a rate category designed for mailers that apply postage using meters rather than stamps (which has cost saving consequences for the Postal Service)[6] and which tend to have demand characteristics that differ from household mailers. Nonetheless, no household mailer is prohibited from investing in a postage meter and using the rate. Indeed, innovations of the type suggested by Stamps.com may pave the way for more to do so.[7] Nor is it probable that household mailers applying stamps are currently similarly situated, from a cost or demand perspective, to the small and medium-sized businesses that use postage meters. Thus, any assertion that the Metered Mail rate category violates Section 403(c) of the PAEA fails at the outset, before even getting to whether there is a legitimate basis for the different treatment.

GCA says that the Postal Service is charging the "household mailer an extra cent" for the benefit of small business mailers. *GCA Comments* at 7. But whether the stamp rate would be any lower if the Metered Mail rate category did not exist is sheer speculation. Indeed, the available evidence -- the experience of Docket No. R2015-4 – strongly suggests that business, not household, mailers would pay more. There, the

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6 In particular, metered mail has substantially lower mail processing costs than stamped mail. *Compare USPS FY14-36.shp14prc.xls (Tab Summary)* (showing Single-Piece Letter mail processing unit cost of 13.10 cents *with USPS FY14-10_FCM_letters.xls (Tab Summary)* (showing total mail processing costs of Metered Letters of 10.772 cents).

7 *Initial Comments of Stamps.com* at 4-6 (Feb. 2, 2015).

Postal Service is narrowing the difference between the stamp and the metered rate from one cent to 0.5 cents, but there is no corresponding *decrease* in the stamp rate *at all*, as would be the case if GCA were correct. Instead, Presort Letters and Cards are bearing the full brunt of the overall increase in an amount far more than the rate of inflation.

Although they have difficulty characterizing the Metered Mail rate as an example of price discrimination of the type prohibited by Section 403(c), APWU and GCA argue whether it is properly included in a "just and reasonable" rate schedule as desired by Section 3622(b)(8) of the PAEA. That is addressed in the following section.

C. The Metered Mail Rate Category Promotes Legitimate Postal Service Objectives And Is Just And Reasonable Consistent With Section 3622(b)

When it established the Metered Mail rate category in Docket No. R2013-10, the Postal Service did not present it as a worksharing discount because applying postage via a meter does not come within the definition of worksharing in Section 3622(e). APWU apparently, if grudgingly, has abandoned any contention that the Metered Mail rate category somehow constitutes a worksharing discount. *APWU Comments* at 8.

Instead, essentially conflating Section 3622(b)(8) with the anti-discrimination provision of Section 403(c), APWU argues that if the Metered Mail rate category is not a worksharing discount, then it would constitute a "preference" for business customers "untethered to any technological efficiency" that lacks any acceptable justification and consequently discriminates unreasonably against "household" mailers in violation of Section 3622(b)(8). *APWU Comments* at 10.

APWU's underlying premise is incorrect. Nothing in the PAEA forbids the Postal Service from setting a price on a basis unrelated to worksharing. Nor does the law contain any requirement that a non-worksharing rate category differential can be justified solely due to technological efficiency. For example, several years ago the Commission approved "density" as a non-worksharing basis for a separate rate category. *See Consideration of Workshare Discount Rate Design*, Docket No. RM2009-3, Order No. 536 at 59-61 (Sept. 14, 2010) (Order Adopting Analytical Principles Regarding Workshare Discount Methodologies).

Instead, Congress in the PAEA gave the Postal Service pricing flexibility to establish rate categories for any legitimate business reason. Indeed, the PAEA's objectives of granting the Postal Service greater pricing flexibility (39 U.S.C. §3622(b)(4)) and to maximize efficiency (39 U.S.C. §3622(b)(1)) would mean little if price differences could be justified only via the straightjacket workshare provisions of Section 3622(e).[8]

The Postal Service's introduction of the Metered Mail rate category in Docket No. R2013-10 implemented the Commission's separate, previous suggestion that the rate would be an appropriate benchmark for Presort discounts. That alone is sufficient

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[8] The Metered Mail rate category unquestionably is compensatory – no one contends that Metered Mail fails to cover its costs (First-Class Single-Piece mail as a product pays an average of 20.8 cents of unit contribution, and Metered Mail probably pays above the average contribution).

rationale for the rate. But the Postal Service also advanced a number of other reasonable grounds for the rate, any of which would sufficiently justify the category.[9]

APWU dismisses those grounds as "conclusory" assertions that do not suffice in light of the decision of the United States Court of Appeals for the District of Columbia Circuit in the *GameFly I* case.[10] But *GameFly I* seems to have little bearing here. The issue in *GameFly I* was the sufficiency of the remedy awarded in a complaint case concerning the Postal Service's discriminatory handling of DVDs from one mailer while refusing to give the same handling to another mailer of DVDs similarly situated, where the remedy misattributed a lingering price difference to the complainant's own choice rather than to the underlying discrimination that forced that choice.[11] *GameFly I* had nothing to do with what constitutes legitimate grounds for setting rates for categories and products, but concerned the Postal Service's unreasonable refusal to extend to GameFly the special manual processing it gave to Netflix.

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9 *Supra* at 4.

10 The APWU's swipe (at 9) at the Postal Service's statement that the experience of foreign posts provides grounds for expecting certain mailer behavior in the United States seems to miss the point completely. The experiences of foreign posts that offer a metered mail rate can provide a reasonable indication of what the Postal Service over time may expect to see from a similar rate category. APWU suggests no reason why mailers in the United States would not respond rationally to comparable incentives here in a manner similar to foreign mailers.

11 The *GameFly I* Court summarized the matter as follows: "The Commission cannot justify the terms of service discrimination its remedy leaves in place (providing manual letter processing to Netflix but not to GameFly) based on the companies' use of different mailers when the use of different mailers is itself the product of the service discrimination."

For its part, GCA argues that under the Section 3622(b)(8) objective of a just and reasonable rate schedule, the Metered Mail rate category is a price discrimination against household mailers that the Postal Service must justify "in terms of benefit to the First-Class mailing community as a whole, or of operating benefits to the Postal Service." *GCA Comments* at 4. It is not clear that this formulates the correct standard. The benefits from the Metered Mail rate category need not be "operating" in nature, unless, say, the reduction in stamp theft or the ongoing retention of profitable mail is considered an "operating benefit." There must be a benefit to the Postal Service, but appropriate benefits need not be limited to some narrow notion of "operating" benefit.

Nonetheless, NPPC agrees with the importance of a "just and reasonable rate structure" and towards that end recommended in its initial comments that the Commission act to reduce the gross inequity in institutional cost contributions imposed upon business mailers by the current First-Class Mail rate structure. Indeed, only two days after GCA submitted its comments in this proceeding, it told the Commission that "equal contribution per piece is the key comparator" between Single-Piece and Presort Mail (*see GCA Comments*, Docket No. R2015-4, at 1). Unfortunately, GCA's comments in this proceeding would worsen, not improve, the situation. Were the Metered Mail rate to be eliminated (or the differential from the stamp rate reduced, as the Postal Service has proposed to do in Docket No. R2015-4), the more than 5-cent gap (or 25 percent more than the Single-Piece Letters/Cards unit contribution – *ACR* at 7) between the unit contribution from Presort and that from Single-Piece mail would increase materially as the effects of the higher benchmark rate ripple through the Presort product.

GCA's attempt to calculate whether the Metered Mail rate has caused stamp mail to convert is premature, out-of-context, and beside the point. *GCA Comments* at 4-6. It is unrealistic to expect substantial conversion in the first months of a new rate, especially when the new rate was swamped by an overall significant rate increase. One would never know, when reading GCA's comments, that the mailers paying the Metered Mail rate saw a significant net rate *increase* in FY2014 because the exigent surcharge approved in Docket No. R2013-11 was implemented simultaneously with the new Metered Mail rate category. Consequently, mailers using meter postage did not receive a decrease, but rather saw their rates rise from 46 cents to 48 cents (while the stamp rose from 46 cents to 49 cents). It is unsurprising that business mailers facing a postage increase mailed fewer letters; however, the exigency surcharge does complicate any analysis of conversion.

Finally, the possible conversion of stamped mail to Metered Mail was only one of several effects that the Postal Service expected that it might see. The Postal Service also expected the Metered Mail rate category to help preserve mail volume and reduce postage stamp theft. The comments of Pitney Bowes provide an estimate of how the Metered Mail rate may already have benefitted the Postal Service by preserving volumes in the only two postal quarters in which it has been in effect.

GCA also argues that the Metered Mail rate category is inconsistent with Section 3622(b)(1), pursuant to which the rate regime should maximize incentives to reduce costs and increase efficiency. *GCA Comments* at 7-8. GCA's comments are premised on an assumption that Section 3622(b)(1) requires mailers to "change" behavior and may not "reward" mailers for doing something that they already do. Subsection (b)(1) is not so limited. Its objective can also be achieved by encouraging mailers to *continue* to engage in cost-reducing and efficient activities as well as promoting new behavior.

More than 5 billion pieces used the Metered Mail rate category in FY2014, and the Postal Service forecasts even more pieces to use the rate in the coming year.[12] Each one of those pieces used or will use more efficient and less costly metered postage payment. Every piece that pays the Metered Mail rate is responding to an incentive to reduce its costs and improve the efficiency of its mail to the maximum extent possible. In addition, the Metered Mail rate provides a more accurate and efficient benchmark for the Presort mail discounts, further promoting efficiency and cost minimization. Pricing that encourages mailers to continue to engage in cost-saving behavior and to remain in the postal system are reasonable and serve the long-term interests of the Postal Service.

Lastly, GCA argues that the Metered Mail rate category poses a threat to the Postal Service's fiscal stability in a manner inconsistent with Section 3622(b)(5). That characterization is simply wrong on its face. The Postal Service's fisc is far better off with Metered Mail in the system, and serving as a benchmark for Presort mail, than if it were to convert to electronic distribution.

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[12] *See* Docket No. R2015-4, USPS R2015-4 CAPCALC-FCM.xls (Tab Single-Piece) Cell D5.

The gist of the criticisms of the Metered Mail rate category is that First-Class business mailers – who already pay far more in unit contribution than household mailers, a status which the rates proposed in Docket No. R2015-4 would make worse – should pay still more, and that the high unit cost/lower contribution and dwindling volume household mail should be protected against anything that might raise their rates. That is not sound ratemaking policy, and that is not consistent with the PAEA. APWU and GCA have provided no basis for the Commission to reach such a conclusion in this Annual Compliance Determination.

IV. CONCLUSION

First-Class business mailers not only pay a grossly disproportionate share of institutional costs; they also face increased costs for declining service and escalating compliance costs. In these circumstances, the notion that household mailers are somehow suffering from discrimination that *favors* business mailers would be laughable were the financial consequences not so dire.

For the foregoing reasons, and for the reasons stated in its previous Comments in this proceeding, the National Postal Policy Council respectfully urges the

Commission to take these Comments into consideration in making its Determination, and to reject the criticisms of the Metered Mail rate.

Respectfully submitted,

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